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No. 94-18

IN THE

Supreme Court of the United States

OCTOBER TERM, 1994

Antonio C. Mastrobuono and Diana G. Mastrobuono,

Petitioners,

v.

Shearson Lehman Hutton Inc., a corporation, and Nick DiMinico,

Respondents.

On Writ of Certiorari to the United States Court of Appeals for the Seventh Circuit

REPLY BRIEF FOR PETITIONERS

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REPLY BRIEF OF PETITIONERS

I.

THE PRINCIPLE THAT THE FAA REQUIRES ENFORCEMENT OF ARBITRATION AGREEMENTS AS WRITTEN REQUIRES ENFORCEMENT OF THE PARTIES' COMPREHENSIVE AGREEMENT TO ARBITRATE, AND PREEMPTS NEW YORK STATE LAW WITHDRAWING THE PARTIES' ABILITY TO AGREE TO ARBITRATE ALL ISSUES, INCLUDING PUNITIVE DAMAGES.

(Reply to Resp. Br., Pt. I, pp. 12-16).

Respondents assert that the FAA requires enforcement of arbitration agreements according to their terms but neither creates new rights nor compels arbitration. (Resp. Br., pp. 12-13). Petitioners do not dispute this principle but respectfully submit that respondents' attempt to apply that principle to the facts presented here rests on a flawed analysis. Respondents' argument narrowly focuses on the New York choice-of-law

provision contained in the Client's Agreement and completely disregards the comprehensive arbitration provision, by which the parties agreed to arbitrate "any controversy arising out of or relating to [the Mastrobuonos'] accounts, to transactions with you, your officers, directors, agents and/or employees for [the Mastrobuonos] or to this agreement or the breach thereof...." That the Client's Agreement also contains a New York choice-of-law provision and, under New York state law, arbitrators cannot award punitive damages, does not detract from the enforceability, as a matter of federal substantive law, of an arbitration clause governed by the FAA, because, as respondents acknowledge, the FAA requires enforcement of arbitration agreements. The arbitration agreement involved here is

extremely broad and does not purport to withhold any matter relating to the Client's Agreement from arbitral consideration or to limit the remedies which the arbitrator may award.

Moreover, respondents argue, "Since the FAA requires enforcement of the designation of New York law in the parties' agreement, the FAA mandates enforcement, not preemption, of the New York rule of [*Garrity*] in this case." (Resp. Br., p. 14). Respondents are incorrect. As discussed at length in petitioners' opening brief, the New York restriction on arbitral authority is in fundamental conflict with the goals of the FAA and embodies the misguided over-protection of judicial jurisdiction which the FAA was enacted to overcome. As this Court has made clear again and again,

state law hostile to arbitration is preempted by the FAA. (See Pet. Br., pp. 18-30). Contrary to respondents' assertions, preemption is equally applicable here, where the law of a state named in a choice-of-law provision is asserted to obviate the enforceability of arbitration agreements by withdrawing arbitral power, arguably by implication, to resurrect anti-arbitration state law and to accomplish indirectly what this Court has indicated may not be done directly.

Respondents' argument is also fatally flawed because it is based on circuitous reasoning which achieves an untenable result. Respondents contend that the parties agreed to a New York choice-of-law provision, thereby incorporating the *Garrity* rule into their agreement, and

that the FAA requires enforcement of the agreement and, therefore, enforcement of the *Garrity* rule. This argument is, however, based on a misapprehension of the content of the New York law which governs by virtue of the choice-of-law clause. Because the agreement here involves interstate commerce, it is ultimately governed by federal law, the FAA. A state choice-of-law clause does not impact or "preempt" the application of federal law. As respondents acknowledge, federal law always applies. (Resp. Br., pp. 19-20, n. 3).

For example, it is undisputed that if New York state law applied to the agreement as a matter of application of conflict-of-law principles, the FAA would preempt application of the New York rule against arbitral awards of punitive

damages. Contrary to respondents' assertions (Resp. Br., p. 21), discussed further *infra*, there is no basis for reaching a different result where New York law applies by virtue of a choice-of-law provision contained in the parties' agreement; the New York law which applies by reason of a choice-of-law clause is the state law not preempted by federal law. To conclude otherwise would render the FAA a nullity and would yield a result wholly contrary to Congress' intent in enacting the FAA by allowing it to be used as a tool to *enforce* rather than overcome state law which expressly withdraws the ability of the parties to agree to arbitral awards of punitive damages and which reserves the right to award punitive damages exclusively to the judicial forum.

II.

THE PARTIES' COMPREHENSIVE AGREEMENT TO ARBITRATE DOES NOT WITHDRAW FROM THE ARBITRATORS THE POWER TO AWARD PUNITIVE DAMAGES.

(Reply to Resp. Br., Pts. IIA and IIB, pp. 17-34).

A. The New York Choice-Of-Law Clause Contained In The Parties' Agreement Does Not Include The *Garrity* Rule; With Respect To Arbitration Agreements Involving Interstate Commerce, The FAA Preempts The *Garrity* Rule.

Respondents argue, "Nothing in the FAA or in any of this Court's decisions under the Act suggests that there is any federal policy that is hostile to choice-of-law clauses or justifies selectively excising legal rules that would normally be within the ambit of a choice-of-law clause." (Resp. Br., p. 17). Petitioners, however, have not suggested that choice-of-law clauses are not enforceable, but that they should be

applied in the manner in which they are typically intended to function. As respondents acknowledge, the function of a choice-of-law provision is to designate the state law that will apply, rather than leave the determination of what state law will apply to the application by the courts (or arbitrators) of conflict-of-law principles. (See Resp. Br., pp. 19-20, n. 3). For this reason, the cases cited by respondents in support of their assertion that, "[i]n the absence of any limiting provisions, it is fundamental that a choice-of-law clause incorporates not only the liability law of the chosen state, but its law relating to remedies, including whether punitive damages are available," are distinguishable. (Resp. Br., p. 25). All of the cases cited involve enforcement of the law of the state named in a choice-

of-law provision rather than the law of *another state*. None of the cases cited addresses the impact of the FAA. Petitioners do not contest that a state may generally limit or preclude the availability of certain remedies. The FAA, however, precludes states from limiting the availability of remedies based on the fact that they are to be determined, pursuant to an arbitration agreement, in an arbitral forum. See *Perry v. Thomas,* 482 U.S. 483, 492, 107 S.Ct. 2520, 96 L.Ed.2d 426 (1987).

Respondents acknowledge, as they must, that a state choice-of-law clause does not impact upon the application of federal law but ignore the import of this acknowledgment. Here, irrespective of the New York choice-of-law provision contained in the parties' agreement, federal law

applies, federal law which establishes "a liberal federal policy favoring arbitration agreements, notwithstanding any state substantive or procedural policies to the contrary." See *Moses H. Cone Hospital v. Mercury Construction Corp.*, 460 U.S. 1, 24, 103 S.Ct. 927, 74 L.Ed.2d 765 (1983).

Nonetheless, respondents assert that federal law does not have any preemptive impact upon state law incorporated into an agreement by virtue of a choice-of-law clause. In support of their argument, respondents cite this Court's decision in *Volt Info. Sciences, Inc. v. Board of Trustees,* 489 U.S. 468, 109 S.Ct. 1248, 103 L.Ed.2d 488 (1989), claiming, "The very point of the *Volt* decision was that the choice-of-law clause incorporated state law principles that would have been

preempted if California law had applied of its own force." (Resp. Br., p. 21). This is simply incorrect. This Court's decision in *Volt* is discussed at length in petitioners' opening brief. (Pet. Br., pp. 44-53). However, it should be emphasized here that at issue in *Volt* were state procedural arbitration rules which the Court determined were "manifestly designed to encourage resort to the arbitral process," not a blanket state law restriction on arbitral authority, like that at issue here.[1] The Court further

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[1] For this reason, whether New York state law encompasses procedural arbitration rules which may or may not encourage resort to the arbitral process is simply irrelevant. (See Resp. Br., pp. 22-23).

Respondents also contend that, "Characterizing the [*Garrity*] rule as 'substantive rather than procedural' makes this an *a fortiori* case for applying *Volt*, because it eliminates any possible ground for treating the rule as outside of the scope of the choice-of-law provision."

concluded that the California arbitration rules did not offend any policy embodied in the FAA and that the parties' agreement to abide by state rules of arbitration could be enforced "without doing violence to the policies behind the FAA." *Volt*, 489 U.S. at 479. The same clearly cannot be said here.

Respondents also argue that they were not required to specify that punitive damages would not be allowed, or to make some other express inclusion of the *Garrity* rule and that such a requirement would contravene the purpose of a choice-of-law clause as a means of incorporating

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(Resp. Br., p. 27). This argument further illustrates respondents' confused reasoning. Petitioners have not suggested that a choice-of-law clause incorporates only state law procedures rather than state substantive law, but, as stated *supra*, where state substantive law conflicts with the FAA, it is preempted.

an entire body of state law. (Resp. Br., pp. 17-20). Under the circumstances presented here, however, such a specific incorporation would be necessary to separately establish an agreement by the parties to forego the availability of punitive damages in order to circumvent the preemptive effect of the FAA on the New York law incorporated into the agreement. It should also be noted that respondents' argument in this regard is, at best, inconsistent; they suggest that a requirement of an express provision relating to the availability of punitive damages would pose significant questions regarding which rules must be expressly referenced and what is the point of a choice-of-law clause if there is an issue as to the state rules of law which it incorporates. (Resp. Br., p. 21). The

issue posed here is not the applicability of some general principle of New York law, but a principle of law which works in tandem with the comprehensive arbitration clause to foreclose the availability of punitive damages in arbitration. Respondents drafted the agreement, including the agreement to arbitrate, clearly with the intention of achieving this "waiver by implication" of any award of punitive damages against it.

Even more inconsistent is the following assertion of respondents:

> The petitioners' position would have the courts bend arbitration agreements in the direction of giving claimants the broadest possible benefits. The utility of arbitration depends on the willingness of parties to submit their disputes to the process. If the judicial approach is to put a thumb on the plaintiff's side of the scale in interpreting the agreement, resort to the process is at least as likely to be deterred

> as encouraged, especially when the remedy at issue gives arbitrators an uncontrolled and unreviewable discretion to assess punitive damages. (Resp. Br., pp. 23-24).

Simply put, respondents drafted the agreement and could have imposed upon petitioners an explicit restriction on the award of punitive damages, as they imposed a comprehensive arbitration agreement. Now, not having achieved the result which they believed they could achieve in their selected forum, respondents should not be heard to assert that they have not been treated fairly or to assert that resort to the arbitral forum [by broker/dealers] will be discouraged because arbitrators are seeking to render appropriate decisions, including decisions in favor of investor plaintiffs where warranted. The flaw in respondents' argument lies precisely in the fact that their

definition of fairness is apparently tied to their ability to prevail whether in the right or the wrong.[2]

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[2] Respondents also assert that permitting arbitrators to award punitive damages would discourage arbitration because it would give arbitrators "an uncontrolled and unreviewable discretion to assess punitive damages." (Resp. Br., pp. 23-24). Respondents' assertion ignores the fact that, in the first instance, they selected the forum. Further, there is no merit to the claim that excessive arbitral awards of punitive damages are "uncontrolled or unreviewable." Although the issue is not presented here, it would appear that where the amount of a punitive damages award was clearly excessive, arbitrary or capricious, it would be subject to review under either 9 U.S.C. §10(a)(2), as demonstrating "evident partiality" on the part of the arbitrators or, as the SEC suggests, under 9 U.S.C. §10(a)(4), as exceeding arbitral power. (SEC Br., p. 20, n. 14).

Respondents' amicus, the Securities Industry Association ("SIA"), attempts to interject an issue relating to possible due process concerns implicated by arbitral awards of punitive damages. (SIA Br., pp. 14-17). In their brief, however, respondents have not asserted that an award of punitive damages would violate their due process rights or claimed that the amount of the arbitrators' punitive

B. As The Seventh Circuit Acknowledged, The New York Choice-Of-Law Clause Is Inconsistent With The NASD Arbitration Rules.

Respondents further argue that the Seventh Circuit correctly concluded that the New York choice-of-law provision was

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damages award is excessive. Because a due process issue has not been raised by the respondents, nor passed upon by the District Court or the Court of Appeals, it is not properly raised by the SIA.

In any event, however, the SIA fails to address the fact that this Court has previously indicated that federal claims, under which treble damages with an acknowledgedly punitive aspect, may be arbitrated. (See Pet. Br., pp. 25-30). Moreover, respondents were given notice from the outset of this litigation that petitioners were seeking punitive damages, and it was the *respondents*, not the petitioners, who compelled arbitration and had a full and fair opportunity to resist petitioners' claim for punitive damages. Further, petitioners' claim for punitive damages was decided by a panel of three arbitrators "which was much less likely than a jury to be swayed by passion and prejudice." See *J. Alexander Securities, Inc. v. Mendez*, 17 Cal.App.4th 1083, 1095, 21 Cal.Rptr.2d 826 (Cal. Ct. App. 1993), *cert. denied*, _____ U.S. _____, 114 S.Ct. 2182, 128 L.Ed.2d 901 (1994).

controlling, notwithstanding provisions of the NASD rules which conflict with New York's prohibition against arbitral awards of punitive damages. The NASD Code of Arbitration Procedure states that it is "prescribed and adopted...for the arbitration of *any dispute, claim or controversy* connected with the business of any NASD member." (*Mastrobuono v. Shearson Lehman Hutton Inc.*, 20 F.3d 713, 717-718 (7th Cir. 1994); Pet. App., pp. 14-15). The Seventh Circuit also acknowledged that the NASD Arbitrators' Manual provides, "Parties to arbitration are informed that arbitrators can consider punitive damages as a remedy." (*Mastrobuono*, 20 F.3d at 717-718 (7th Cir. 1994); Pet. App., p. 15). Respondents, however, argue that the only potentially applicable provisions of the NASD Code Of Arbitration (Sections

12(a) and 41(e)) are silent with respect to punitive damages and that the NASD Arbitrator's Manual is inapplicable because it is not incorporated into the Client's Agreement, is "merely a compilation of general information for the benefit of arbitrators," compiled by the Securities Industry Conference On Arbitration, and is not part of the NASD's rules of procedure. (Resp. Br., pp. 31-32).[3] The "any dispute, claim or controversy" language of Section 1 of the NASD Code of Arbitration Procedure is, however, clearly broad enough to encompass

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[3] The Seventh Circuit also apparently concluded that NASD Rule Of Fair Procedure 21(f)(4), which provides that "[n]o agreement shall include any condition which...limits the ability of the arbitrators to make any award" was applicable but concluded, nonetheless, that the New York prohibition against arbitral awards of punitive damages controlled. (*Mastrobuono*, 20 F.3d at 18; Pet. App., p. 17).

an award of punitive damages, and the provision of the NASD's Arbitrator's Manual clarifies that arbitral awards of punitive damages are contemplated under the NASD Code of Arbitration Procedure. Accordingly, under the federal policy requiring the resolution of any doubts concerning the scope of arbitral issues in favor of arbitration (*Moses H. Cone,* 460 U.S. at 24-25), as well as well-established contractual principles requiring the resolution of ambiguity against the drafter of a contract (*U.S. v. Seckinger,* 397 U.S. 203, 208, 90 S.Ct. 880, 25 L.Ed.2d 224 (1970); *Jacobson v. Sassower,* 66 N.Y.2d 991, 992, 499 N.Y.S.2d 381, 489 N.E.2d 1283 (N.Y. 1985)), the Client's Agreement should be read to permit an award of punitive damages.

Respondents' arguments to the contrary resort again to circuitous reasoning, arguing that the NASD rules require enforcement of the arbitration agreement, which in this case contains a New York choice-of-law clause and a provision that it is to be governed by the rules of the NASD or the Boards of Directors of the New York Stock Exchange ("NYSE") or the American Stock Exchange ("ASE"), as the customer may select. Respondents, however, cannot obviate the ambiguity of the Client's Agreement by focusing exclusively on one provision (the New York choice-of-law provision) and ignoring the provision giving rise to the ambiguity (the provision providing for arbitration pursuant to the rules of the NASD, the NYSE or the ASE.)

Further, respondents attempt to distinguish the decisions of the First, Eighth, Ninth and Eleventh Circuits, permitting arbitral awards of punitive damages, notwithstanding the inclusion of choice-of-law clauses naming states which did not permit arbitral awards of punitive damages, asserting that in each of those cases "the decision relied on the existence of AAA Rule 43 as overriding or at least creating a contradiction with the choice-of-law clause." (Resp. Br., pp. 33-34). Although the Courts of Appeal considered the fact that the agreements at issue provided for arbitration pursuant to the rules of the AAA in *Raytheon Co. v. Automated Business Systems, Inc.*, 882 F.2d 6 (1st Cir. 1989),[4] *Lee v. Chica*, 983 F.2d

[4] In *Raytheon*, the First Circuit noted that the appellant had conceded that federal law controlled but, independent of this, adopted the view that "the contract's choice-of-law provision does not require us to determine the punitive damages question by looking to the law of the chosen forum (in this case, California). Rather, we, like [other courts], look to federal common law for our answer." *Raytheon*, 882 F.2d at 11, n. 5. The Court also concluded that the parties' adoption of the AAA rules further supported this conclusion.

883 (8th Cir. 1993), *cert. denied*, ___ U.S. ____, 114 S.Ct. 287, 126 L.Ed.2d 237 (1993), *Todd Shipyards Corp. v. Cunard Line, Ltd.*, 943 F.2d 1056 (9th Cir. 1991), and, *Bonar v. Dean Witter Reynolds, Inc.*, 835 F.2d 1378 (11th Cir. 1988), the Courts of Appeal found, apparently independently of that fact, that the FAA preempted the state law claimed to prohibit an arbitral award of punitive damages.

III.

THE ARBITRATORS DID NOT EXCEED THE SCOPE OF THEIR AUTHORITY IN AWARDING PUNITIVE DAMAGES AND THE SEVENTH CIRCUIT IMPROPERLY VACATED THE AWARD OF PUNITIVE DAMAGES UNDER SECTION 10(A)(4) OF THE FAA.[5]

(Reply to Resp. Br., Pt. III, pp. 34-42).

Respondents contend that the SEC's argument that the Seventh Circuit (and the District Court) failed to give appropriate deference to the arbitrators' construction to the contract and that a claimed error in the arbitrators' interpretation of the contract does not constitute a basis for vacating their award, does not apply to

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[5] Petitioners' submit that this Court may appropriately consider the ground for reversal urged by the SEC (SEC Br., pp. 12-28), although not pressed by petitioners in their opening brief, it was raised in the courts below and has been presented by the SEC in their brief, with respondents having had the opportunity to respond, and is now adopted by petitioners as an alternative basis for reversal of the Seventh Circuit's decision.

the facts of this case. (Resp. Br., pp. 34-35). Respondents argue that "the arbitrators did not 'interpret the contract' for this purpose but instead found it unnecessary to consider the contract's language." (Resp. Br., p. 35). In support of this argument, respondents reference the fact that in their award, the arbitrators stated that the authority for their award of punitive damages could be found in Claimants' Response to Shearson's Brief In Opposition to Punitive Damages ("Claimants' Response"). In constructing their argument, however, respondents have taken from its context a single argument made in Claimants' Response and have disregarded other arguments made by petitioners' in support of the arbitrators' power to award punitive damages notwithstanding the New

York choice-of-law clause contained in the Client's Agreement. In response to respondents' citation to the decision in *Barbier v. Shearson Lehman Hutton Inc.*, 948 F.2d 117 (2nd Cir. 1991), petitioners argued:

> Arbitration panels are thus not absolutely required to adhere to the letter of cases such as [*Barbier*]. This panel can and should do justice for the parties and apply the rules of law and equity as the arbitrators see them. The panel's decision should reflect the spirit rather than the letter of the law and of the parties' agreement. (Motion To Partially Vacate Award, Dkt. No. 58, Exhibit C, p. 2).

Additionally, petitioners cited *Willoughby Roofing & Supply v. Kajima International, Inc.*, 598 F.Supp. 353 (N.D. Ala. 1984), wherein the District Court concluded that a choice of law provision in a contract governed by the FAA designates only the substantive law that

the arbitrators must award in determining whether the conduct of the parties warrants an award of punitive damages but does not deprive the arbitrators of their authority to award punitive damages. (Motion To Partially Vacate Award, Dkt. No. 58, Exhibit C, p. 2). Petitioners also argued, among other things, that punitive damages awards were contemplated under the NASD Rules of Fair Practice and Arbitrator's Manual. (Motion To Partially Vacate Award, Dkt. No. 58, Exhibit C, p. 3). Under these circumstances, there is simply no basis for respondents' argument that the arbitrators did not base their conclusion that they could appropriately award punitive damages upon their interpretation of the Client's Agreement.

Further, contrary to respondents' claim that any purported interpretation of

the agreement which found that the *Garrity* rule was not controlling is outside of the bounds of a fair construction of the agreement (Resp. Br., p. 36), the arbitrators' construction of the contract was reasonable and should have been upheld by the Seventh Circuit. As discussed *supra*, the reference to the NASD rules contained in the parties' agreement gave rise to an ambiguity properly the subject of resolution by the arbitrators, and, just because the arbitrators failed to accept the interpretation asserted by respondents, does not render their construction untenable, unreasonable or subject to *de novo* review.

In support of their argument, respondents assert that this Court has "made clear that questions whether the parties have agreed to arbitrate and, if

so, what issues are included within that agreement, are for the court to decide, not the arbitrator." (Resp. Br., p. 40, citing *AT & T Technologies, Inc. v. Communications Workers of America,* 475 U.S. 643 (1986)). As the SEC points out in its brief, however, questions concerning the scope of arbitral authority with regard to matters conceded to be arbitral must be distinguished from issues relating to whether a particular claim is to be resolved by the arbitrator or the court. (SEC Br., pp. 17-18, n. 13). For example, a question whether an action brought by one of the petitioners for personal injuries sustained while on Shearson's premises while meeting with DiMinico with regard to an investment pursuant to the Client's Agreement might present a question of whether the action

is arbitrable. Such a question would be subject to judicial determination. On the other hand, the controversy at issue here, respondents' improper conduct in handling petitioners' account, clearly falls within the scope of the arbitration agreement, which provides for the arbitration of "any controversy arising out of or relating to [the Mastrobuonos'] accounts, to transactions with you...or to this agreement or the breach thereof..." (Pet. App., p. 44).

Moreover, here, petitioners' claims were submitted to arbitration at the behest of respondents, who, at the time they sought to compel arbitration, did not suggest that any of petitioners' claims were not arbitrable on the basis that punitive damages were requested or on any other basis. Now that the arbitrators, on

the basis of their construction of the contract which is neither unreasonable nor ignores the plain language of the contract,[6] have determined that they could properly award punitive damages, their determination should have been reviewed deferentially. Application of any other standard would render arbitration useless as a method of dispute resolution and would permit litigants, like respondents here, to insist on arbitration and, when dissatisfied with the results of the arbitration, to turn to a *de novo* ruling

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[6] If the language expressly prohibited an award of punitive damages, and the arbitrators nonetheless awarded punitive damages, then it would be clear that they had exceeded their power. Here, however, the arbitrators were entitled to construe the New York choice-of-law provision as designating the substantive law they were to apply in determining whether respondents' conduct warranted a punitive damages award, as did the Court in *Bonar*.

in a judicial forum in the hope that they will have better luck there.

IV.

PETITIONERS HAVE NOT WAIVED THEIR RIGHT TO OBTAIN PUNITIVE DAMAGES. THEIR AGREEMENT TO A NEW YORK CHOICE-OF-LAW CLAUSE AND A COMPREHENSIVE ARBITRATION PROVISION DOES NOT CONSTITUTE A VOLUNTARY AND INTENTIONAL RELINQUISHMENT OF A KNOWN RIGHT.[7]

Respondents initially argue that respondents had no right to recover

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[7] The SIA suggests that this definition of waiver as a voluntary relinquishment of a known right is not applicable here, stating, "While that standard may govern some waivers of constitutional rights, we know of no case invoking it to measure the validity of a commercial contract between private parties, and petitioners have cited none." (SIA Br., p. 22). The SIA is mistaken. As cited in petitioners' brief, in *Bonar*, the Eleventh Circuit applied the above-referenced standard in circumstances essentially identical to those presented here and concluded that there was no waiver. (Pet. Br., pp. 60-61). See also, *J. Alexander Securities, Inc., supra,* 17 Cal.App.4th 1083 at 1093-1094.

punitive damages in the first instance and, therefore, that they did not "waive" any such right, arguing, "If the right is supposedly conferred by some other state, what state - any state whose law happens to favor the petitioners' position?" (Resp. Br., pp. 42-44). Respondents further contend that petitioners "obviously do not mean [that they had such a right under] New York law, because New York law under the circumstances of this case provides that there is *no* right to punitive damages." (Resp. Br., p. 43; emphasis in original). Throughout the proceedings below petitioners asserted a right to recover punitive damages under their common law and statutory claims for, among other things, breach of fiduciary duty and violation of the Illinois

Consumer Fraud And Deceptive Practices Act.[8]

Respondents' argument confuses a right to recover punitive damages under New York law, which, at least with regard to petitioners' common law claims, supplied the substantive law that the arbitrators were required to apply in determining whether the conduct of the parties warranted an award of punitive damages (see *Bonar*, 835 F.2d at 1387), with a right to obtain an award of punitive damages in an arbitral forum.[9]

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[8] Respondents did not contest petitioners' ability to state claims under the Illinois Consumer Fraud And Deceptive Practices Act or under the Texas Deceptive Trade Practices-Consumer Protection Act, which permits the award of treble damages.

[9] It is not at all clear, as respondents argue, that "If the choice-of-law clause adopted the law of, say, Washington or Nebraska, states that do not allow punitive damages at all, petitioners' argument would be the same."

The decision relied upon by respondents throughout their brief and presumably the basis for their assertion that New York law does not afford a right to punitive damages under the circumstance presented, *Garrity v. Stuart*, 40 N.Y.2d 354, 386 N.Y.S.2d 831, 353 N.E.2d 793 (1976), did not hold that punitive damages could not be awarded under New York law, only that the courts had the exclusive power to award such damages. Further, respondents

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(Resp. Br., p. 44). Here, it is uncontested that New York law permits judicial awards of punitive damages. The basis of the Mastrobuonos' waiver claim is that they had an existing right to punitive damages under New York law, which respondents assert has been implicitly defeated by the Mastrobuonos' agreement to a comprehensive arbitration clause - it is the claimed tandem operation of the New York choice-of-law clause, with the general agreement to arbitrate, to destroy any right to punitive damages in any forum, which the Mastrobuonos assert is unconscionable.

have not contended in the proceedings before the District Court, the Seventh Circuit, or in this Court, that their conduct was not sufficiently egregious to warrant an award of punitive damages.

Respondents' suggestion that petitioners' have failed to appropriately preserve their argument that, if the New York choice-of-law clause and comprehensive arbitration clause are to be held to effect a waiver of any right to punitive damages, the Client's Agreement is unconscionable, also lacks merit. (Resp. Br., p. 45). Petitioners' argument is a corollary to their argument that there was no waiver, which has been pressed throughout the proceedings.

Nor can respondents defend against the unconscionability of their claimed "waiver by implication" by asserting there

is no separate action for punitive damages (Resp. Br., p. 46); the assertion that the Mastrobuonos are prohibited from seeking punitive damages in any forum is, after all, the very heart of the unconscionable nature of respondents' argument.

CONCLUSION

For the foregoing reasons, petitioners respectfully request that this Court reverse the judgment of the Seventh Circuit Court of Appeals and remand this cause for confirmation of that portion of the arbitrators' award awarding petitioners punitive damages in the amount of $400,000 or, in the alternative, for a trial before the District Court on the amount of punitive damages or, in the further alternative, for a trial on petitioners' statutory and common law

claims giving rise to their claims for punitive damages.

Respectfully submitted,

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